T&E COMMITTEE #2
October 21, 2010

MEMORANDUM

October 19, 2010

TO: Transportation, Infrastructure, Energy, and Environment Committee

FROM: Keith Levchenko, Senior Legislative Analyst

SUBJECT: FY12 Washington Suburban Sanitary Commission Spending Control Limits

FY12 Spending Control Limits Summary

	WSSC "Base Case"	CE Recommendation*	Prince George's**
New Debt:	**$325.285 million**	**$325,285 million**	**$325.285 million**
Debt Service:	**$196.290 million**	**$196.290 million**	**$196.290 million**
Total W/S Operating Exp.:	**$579.600 million**	**$569,513 million**	**$560.552 million**
Maximum Avg. Rate Increase:	**12.0 percent**	**9.9 percent**	**8.0 percent**
Unspecified Reductions from Base Case:	- -	$10.087 million	$19.052 million
Avg. Residential Monthly Impact:	$7.19	$5.92	$4.78

Council Staff Recommendation: Concur with CE Recommendation

* CE Transmittal memorandum attached on ©6-7

**Reflects Transportation, Housing and Environment (THE) Committee Recommendation (Full Council action scheduled for 10/1910)

The following officials and staff are expected to attend this meeting.

WSSC

Commission Vice Chair Roscoe Moore
Commissioner Adrienne Mandel
Jerry Johnson, General Manager/CEO
Thomas C. Traber, Chief Financial Officer
Sheila S. Cohen, Budget Group Leader

Executive Staff

John Greiner, Office of Management & Budget
David Lake, Department of Environmental Protection

Background

- Annual process was established in April 1994 via resolution by both Councils. Goal is for both Councils to agree upon certain budgetary limits by November 1 of each year.

- Based on a multi-year planning model, a strategy to stabilize annual rate increases over time, and holding customer fee-supported debt service below 40 percent of the operating budget.

- 4 limits
  - Maximum Average Rate Increase
  - Debt Service
  - New Debt
  - Total Water and Sewer Operating Expenses

- Limits provide direction to WSSC as to what to request, <u>but do not create a ceiling (or a floor) as to what the Councils may jointly approve later.</u>[1]

- Process has generally worked well over the past 15 years although Councils did not agree on limits in FY02, FY06, and FY09 and FY10 and FY11. Even in years when there was not agreement, the process provided a rate increase range for WSSC to build its budget.

- Debate focuses on the average rate increase for the coming year and the rate implications for the out years. The other limits are then adjusted to take into account the impacts of the rate decision.

Schedule

- Bi-County Working Group Meetings: September 8, and September 22
- County Executive Recommendation: received October 4
- MC Council Public Hearing: October 5
- T&E Committee Discussion: October 21
- MC Council Action: October 26

The goal of the spending control limits process is to reconcile both Councils' actions (if necessary) by November 1 of each year so that WSSC can build the approved limits into its Operating Budget Public Hearing Draft, which is released by January 15 each year. WSSC must transmit an Operating Budget to both counties by March 1 of each year.

Spending Control Limits History

The following chart presents the rate increase limits agreed upon by both Councils (unless otherwise noted) since FY96 and the actual rate increase later approved for each fiscal year.

[1] State law defines the annual WSSC Proposed Budget as the "default" budget should the Montgomery and Prince George's County Councils not agree on changes. Therefore the limits are an important first step to define proposed budget parameters that are acceptable to both Councils.

WSSC Annual Rate Increase History

Fiscal Year	Rate Increase Approved* Limit	Actual
FY96	3.0%	3.0%
FY97	3.0%	3.0%
FY98	3.0%	2.9%
FY99	2.0%	0.0%
FY00	1.5%	0.0%
FY01	0.0%	0.0%
FY02*	2.0%	0.0%
FY03	0.0%	0.0%
FY04	0.0%	0.0%
FY05	3.0%	3.0%
FY06*	2.5%	2.5%
FY07	3.0%	3.0%
FY08	5.3%	6.5%
FY09*	9.7%	8.0%
FY10*	9.5%	9.0%
FY11*	9.9%	8.5%

*No agreement was reached in FYs 02,06,09,10, and 11. Limits shown for those years reflect Montgomery County Council recommendations.

- FY99-04 – Six straight years of no rate increase as WSSC implemented its Competitive Action Plan (CAP) effort which resulted in a reduction in approximately 1/3 of its workforce (657 positions). WSSC's Retirement Incentive Program (RIP), and additional revenue from the System Development Charge, which the General Assembly expanded in 1998, also tempered WSSC's rate-supported budget.

- FY05 through FY07 saw inflationary level rate increases in the range of 2.5% and 3.0%.

- From FY08 through FY11, the Councils approved rate increases at levels not seen since the early 1990s. These increases were needed because WSSC's water production has been largely flat in recent years even while expenditure pressures have exceeded inflation in areas such as: debt service (to cover many capital needs including WSSC's need to ramp up WSSC's water and sewer main reconstruction efforts and its large diameter water main inspections, repairs, and monitoring program) as well as many operating cost areas including: chemicals, heat, light, and power, regional sewage disposal, and benefits and compensation.

- Infrastructure Fee Debate - During the FY09 budget process, the issue of creating a dedicated fee to accelerate WSSC's water and sewer main reconstruction program was discussed but no fee was ultimately proposed by WSSC. A bi-County Working Group was established to study the issue. The group met several times and considered a number of options related to the creation of a dedicated fee. However, for FY11 no fee was ultimately pursued by WSSC nor approved by either Council. The Bi County Working Group was reassembled this past summer to consider the issue again.

General Issues

Economic Indicators

Each year the Council considers the bi-county economic context in order to place the concept of affordability in clearer perspective. The Council's most recent update on economic indicators was on September 28.

While the national economic recession officially ended in June 2009, 15 months ago, unemployment remains a serious problem. The national rate is currently 9.6 percent. A broader measure that includes underemployed and discouraged workers is 16.7 percent. The County rate, currently 5.5 percent, is well below the national or the State rate (7.3 percent), but it was just 2.5 percent in November 2007 and, until January 2009, had not reached even 4 percent at any time in at least 20 years. Resident employment in the County, at just under 484,000, is 4,500 less than one year ago and 22,400 less than four years ago.

Sales of existing homes, which fell by more than half between 2004 and 2008, rose in 2009 with the first-time homebuyers' credit but are expected to fall again in 2010, partly because of the credit's expiration. Prices, which fell 8.4 percent in 2008 and 13.8 percent in 2009, are expected to rise by less than 1 percent in 2010. Residential and non-residential construction starts are up sharply but from a very low base. Office vacancy rates are now at 11.7 percent, up from 6.5 percent four years ago. Inflation is currently running at an annual rate of less than 2 percent.

Regarding other pressures on the disposable income of County residents, energy costs remain a key factor. Gasoline prices have fluctuated but remain much higher than in recent years. Significantly higher costs for heating and electricity will also persist. Rising health insurance costs are another factor.

In the context of the spending control limits discussion, it is important to keep in mind current economic conditions and their impact on WSSC ratepayers, especially in the context of potential water and sewer rate increases and the cumulative impact on ratepayers of these increases combined with possible increases in other County taxes and fees.

Multi-Year Context

While the spending control limits process is an annual process, the bi-county Working Group takes a multi-year look at trends. The outyear estimates help staff identify issues that could arise in future years. For instance, rate increases in the first year help improve WSSC's fiscal situation in future years by increasing WSSC's base revenues. Conversely, deferring rate increases to future years, or using one-time revenue to reduce a rate increase in the first year, increases future fiscal challenges since the revenue base is lower in future years.

However, with flat water and sewer consumption revenue combined with ongoing capital needs (and corresponding increases in debt service requirements) as well as increased costs for many operating categories, WSSC continues to face significant fiscal challenges.

FY12 Spending Control Limits Base Case Summary

For the upcoming budget, WSSC staff prepared a base case spending control limits scenario (see ©1-3) based on its latest projections of revenue and expenditures and the General Manager's initial considerations regarding current programs and potential new and expanded programs. This base case scenario assumes the following limits:

WSSC Staff "Base Case" Scenario

New Debt:	**$325.285 million**
Debt Service:	**$196.290 million**
Total W/S Operating Expenses:	**$579.600 million**
Maximum Average Rate Increase:	**12.0 percent**[2]

The revenue and expenditure assumptions are described in further detail later. In short, this scenario would:

- Fund the FY12-17 WSSC CIP as recently transmitted, including modest increases in the water and sewer main reconstruction programs.
- Fund a "Same Services" Budget including the next phase of funding for GASB 45 as well as the EAM/ERP IT project.
- Include known major cost increases in the budget (such as regional sewage disposal)
- Assume cost increases for salary and wages that assume COLAs increments and performance pay for WSSC employees.
- Assume a 5% increase in "all other" costs.
- Include some new and expanded programs totaling $6.6 million (in operating costs) and 52 new positions. (see ©5 for summary listing)

The base case scenario results in a funding gap of approximately $56.8 million which translates to a 12 percent rate increase (a $7.19 increase per month to an average residential bill). Future year increases under this scenario would be lower (9.1% in FY13, 8.5% in FY14, 6.3% in FY15, 6.6% in FY16, and 6.3% in FY17).

Also of note is that the debt service to budget ratio would creep up from 33.9% in FY12 to 41.4% in FY17 under the base case. As mentioned earlier, one of the goals of the spending control limits process is to keep debt service below 40% of the budget. However, growth in debt-related spending (for both above-ground and below-ground infrastructure) is causing this ratio to increase over time. **This debt service ratio trend is one reason WSSC has reassembled the Bi-County Infrastructure Working Group to consider new strategies for addressing infrastructure needs over the next 10 to 20 years.**

[2] The elements of the rate increase in the Base Case are itemized on ©4.

Building the Base Case Scenario

The first step the Working Group took in reviewing spending control limits and the base case scenario was to review the major revenue and expenditure assumptions for WSSC. Many of these items are the same as in past years. These assumptions involve various inflators assumed in categories such as salaries and wages, construction inflation, Blue Plains operating costs, and others.

While one can debate particular budget assumptions, the Working Group was satisfied that the assumptions used are reasonable based on current information. It should also be noted that marginal changes in the assumptions are not likely to greatly affect the results of the different scenarios. As discussed later, potential expenditure reductions are identified that would affect these assumptions are considered.

These assumptions were used by WSSC staff to develop the "base case scenario" and are presented on ©1 and are discussed in more detail below.

Fund Balance and Rate Stabilization

Each year, WSSC carries over fund balance from the prior year. The FY10 carryover into FY11 is estimated to be about $48 million. The following chart shows how WSSC is proposing to allocate these dollars.

Table 7:
Estimated FY10 Excess Fund Balance Calculation (in $000s)

FY10 Carryover	**48,014**
FY10 Reserve Requirement	26,500
Increase Reserve (for FY11)	1,500
FY11 use of fund balance for EAM/ERP	1,681
Unallocated Reserve (end of FY10)	**18,333**

The first claim on the reserve is for continuing the reserve into FY11 ($26.5 million plus an additional $1.5 million to increase the reserve to $28.0 million). Another $1.7 million is assumed in the FY11 budget to offset a portion of WSSC's EAM/ERP project costs.

Several years ago, WSSC recommended allocating excess fund balance to increase the designated reserve over time from 5 percent up to 10% of operating revenues. This goal is desired based on discussions with rating agencies and WSSC's interest in having sufficient working capital to overcome a potential short-time revenue shortfall. Last year, the Council agreed to a similar goal for its Tax-supported Fund Balance.

For FY12, the $28.0 million reserve would be approximately 5.6 percent of total revenues. Given the recent rate increases and likelihood of future rate increases, WSSC is not gaining ground on its 10% goal with its annual $1.5 million bump-up in its reserve and is still about $19 below its 10% goal. Since WSSC still has substantial reserves (about $150 million) in its General Bond Debt Service (REDO) account (which it draws down each year to buffer rates), WSSC believes the 10% general reserve goal is not critical to achieve immediately. However, as the REDO dollars are drawn down, the general reserve should be brought up.

The excess fund balance available for FY12 uses is estimated at $18.3 million. This amount is greater than last year's excess balance (about $3.2 million). The surplus is the result of several factors including: lower than expected interest rates (reducing the cost to borrow money for the CIP), no mid-year requirements on the reserve (unlike in FY09 when WSSC had to absorb unbudgeted cost increases in past years chemicals, fuel, street repairs, and biosolids) and delays in some program expenditures (such as EAM/ERP).

WSSCs Base Case assumes to use $7.5 million of the excess fund balance to increase the reserve over the next two years and begin to get closer to a 10% fund balance. Council Staff concurs with this approach.

Council Staff believes the remaining balance, $10.8 million, should be targeted toward one-time or non-recurring costs (rather than rate relief). As assumed for FY11, excess fund balance could continue to be used to partially cover EAM/ERP project costs.

Revenues

Overall, funds available are expected to be down from FY11 by approximately $7.5 million as shown on the following chart. This revenue drop is equivalent to approximately a 1.6 percent rate increase.[3]

WSSC Funds Available (FY11 through FY12)

Revenue	FY11	FY12	change	% change
Water and Sewer Rate Revenue	**478,818,000**	**471,636,000**	**(7,182,000)**	**-1.5%**
Interest Income	**4,000,000**	**4,000,000**	**-**	**0.0%**
Account Maintenance Fee	**22,850,000**	**22,850,000**	**-**	**0.0%**
Other Fees	**8,081,000**	**8,176,000**	**95,000**	**1.2%**
Miscellaneous and Adjustments	**29,126,000**	**26,053,000**	**(3,073,000)**	**-10.6%**
- Miscellaneous	13,547,000	12,760,000	(787,000)	
- SDC Debt Service Offset	2,398,000	2,293,000	(105,000)	-4.4%
- Reconstruction Debt Service Offset	11,500,000	11,000,000	(500,000)	-4.3%
- Use of Fund Balance				
- One-Time Rate Reduction	-	-	-	n/a
- EAM/ERP	1,681,000	-	(1,681,000)	-100.0%
Funds Available	**542,875,000**	**532,715,000**	**(10,160,000)**	**-1.9%**
	equivalent rate increase:		2.16%	

The decline in revenue is primarily the result of continued flat water consumption levels.

WSSC's most important revenue-related assumption is its estimated water production in millions of gallons per day (mgd). WSSC produces approximately 170 million gallons per day (62 billion gallons per year). This production (minus unbilled water), multiplied by a billing factor, determines water and

[3] For FY12 each 1% increase in rates raises approximately $4.72 million in revenue.

sewer rate revenue. This revenue is approximately 90% of all WSSC revenue. On average, every 1 million gallons per day (mgd) produced provides approximately $2.8 million in annual revenue.

WSSC staff are assuming water production to be the same for FY12 (170 million gallons per day, mgd) as assumed in FY11 with slight increases assumed in the out years (based on gradual increases in the customer base). In fact, over the past 15 years, WSSC's water production growth has been nearly flat (increasing about 1.4% in total over that time) even as the population served has increased by about 20 percent.[4]

However, water production is extremely sensitive to various factors, such as weather conditions and customer choices. WSSC's graduated rate structure (in which the more water one uses, the more one pays for all water used) provides a major conservation incentive and WSSC's flat water production, even as the number of customers has increased, may be reflective of successful long-term water conservation efforts in the region.

For FY10, average daily water production averaged 168.7 mgd which was 1.3 mgd below original budget assumptions (although a significant increase over the actual FY09 average daily production level of 162.3 mgd).

Overall, WSSC's revenue trends (putting aside the use of fund balance) continue to be flat. Combined with the adjustments to revenue, a rate increase of 2.16 percent is needed just to cover revenue trends between FY11 and FY12.

With regard to rate revenues, the WSSC customer base is increasing slightly but the billing factor appears to be falling slightly. Absent new revenue sources, future rate revenue is also likely to be modest or flat, given the minor increases in water production expected for the next six years. As a result, inflationary pressures alone result in additional rate increase pressure for FY12 and the foreseeable future.

Expenditure Assumptions

Expenditure assumptions include both debt-related assumptions (interest rates, construction inflation, completion factors) to meet WSSC's Proposed FY12-17 CIP and ongoing operating cost assumptions (Salary and Wage increases, energy, Blue Plains operating charges, "All Other," etc.). These assumptions are noted on ©1 and are similar to assumptions presented during last year's review and are either consistent with historical levels of increase in these areas or are based on locked-in rates (such as energy costs).

In past years, PAYGO has been allocated with excess fund balance and with some rate revenue in order to try to bring down the debt service ratio to budget. However, fiscal pressures and relatively low interest rates have made PAYGO a less appealing option in recent years. No PAYGO is assumed in the spending control limits forecast for FY12 and beyond.

---

[4] Complicating any projection of water production revenue is WSSC's graduated rate structure and the fact that in any given year, the average mix of customers at different rate levels may change.

The salary and wages rate of increase assumed for FY12 (5%) is greater than the 2% assumed in the FY11 spending control limits last year but similar to levels assumed in prior years. This increase would accommodate cost of living adjustments as well as increments plus flexible worker pay.

The Approved FY11 WSSC budget (consistent with other agency budgets) did not include cost of living adjustments (COLAs) for employees. For FY12, the 5% increase would provide for COLAs. Assuming WSSC's compensation approved for FY12 will be kept comparable to other agencies and given the continued difficult fiscal conditions assumed for FY12 across Montgomery County's agencies and in Prince George's County, **a lower assumed rate of increase for salary and wages appears may be reasonable.**

Benefit costs are included in the "All Other" expense category. During the annual operating budget review, the MFP Committee reviews all of the County agency compensation and benefit assumptions with the intent of treating each agency equitably.

Energy costs are expected to increase about 3.4% from FY11 to FY12. These costs are based on actual energy contracts and expected energy usage. WSSC is experiencing an increase in its energy requirements as a result of the implementation of a UV process at its water filtration plants but these costs are offset partially by lower energy costs per KWh.

The Blue Plains regional sewage disposal costs are expected to increase about 3.7% from FY11.

The multi-year implementation of GASB 45 (on an 8 year phase-in) requires an additional $1.0 million added to the base budget in FY12 (with an additional $1.0 million to be added in FYs13-15).

With the exception of the cost increases noted above, "All-Other" costs are assumed to go up 5.0% per year. This is the same increase as assumed last year. Within this category are health care costs as well as employee benefits and regulatory compliance costs (including SSO compliance).

For comparison purposes, the CPI-U for the DC area has been flat over the past year (from July 2009 to July 2010).

Overall, the expenditure assumptions noted above result in a rate increase requirement of about 8.9 percent. Combined with the rate impact of reduced funds available, the rate increase requirement to meet the requirements noted above is about 10.6%.

Finally, WSSC did an initial review of its needs for new and expanded programs. Many of these programs relate to mandates, such as the SSO consent decree, or are needed to expand infrastructure replacement/repair efforts. The total FY12 operating expense impact of these efforts is estimated at $6.6 million with a rate impact of about 1.4 percent. A summary is attached on ©5.

Combining the rate increase requirements to address the reduction in funds available for FY12, the expenditure inflators for FY12, plus the new and expanded programs, the total rate increase requirement is 12 percent.

Alternative Scenarios

As in past years, the bicounty working group developed a number of scenarios based on varying rate increases in FY12.

The following chart summarizes the revenue/expenditure gaps (Column D) at different assumed rate increases (Column A), and the ratepayer impact (Column D). As shown on the chart, a 12% rate increase (the base case assumption) results in no gap. Any rate increase below 12% will result in a gap from the base case that must be addressed either through increased revenues or decreased expenditures.

For reference, each 1% added to the rate provides approximately $4.4 million in revenue to the budget. Alternatively, each 1% reduction in the rate removes $4.4 million in revenues for that year and future years. Each 1% rate increase results in about a 60 cent monthly impact to the average residential customer.

Summary of Impacts At Different Rate Increase Levels

A Scenario	B FY12 Rate Increase	C Revenue Generated	D Base Case Gap	E Ratepayer Impact*
Base Case Gap>>>	0.00%	-	**56,778,000**	
	1.00%	**4,715,780**	52,062,220	$0.60
Rev. Adjustments>>>	2.16%	10,186,090	46,591,910	$1.29
Rev. Adjust.+Debt Serv./Reg Sewage Disp/Energy	7.36%	34,708,150	22,069,850	$4.40
Prince George's County (TH&E Committee Recommendation)	8.00%	37,726,250	19,051,750	$4.78
FY11 Rate Increase>>>	8.50%	40,084,140	16,693,860	$5.08
CE Recommended>>>	9.90%	46,691,420	10,086,580	$5.91
"Same Services plus CIP">>>	10.64%	50,157,990	6,620,010	$6.35
Base Case (incl. new and expanded)>>>	12.04%	56,778,000	-	$7.19

*Monthly impact based on avg. usage of 210 gallons per day and account maintenance fee of $11 per quarter

Column A shows how different levels of rate increase relate to the revenue and expenditure assumptions discussed earlier. For example, a 2.16 percent rate increase is required to cover estimated revenue adjustments between FY11 and FY12. A 7.4 percent rate increase is needed to cover the revenue adjustments plus several of the major cost areas. The rate increase goes up to 10.6 percent to cover a "same services plus CIP" budget (i.e. all of the inflators assumed in the Base Case plus debt service assumed in the recently proposed FY12-17 CIP). The 12.0 percent rate increase would also cover new and expanded programs that WSSC has identified (see ©5 for details). WSSC has provided a chart on ©4 that shows how each major cost and revenue item builds into the 12.0 percent rate increase.

Closing the Gap

As noted earlier, any rate increase below 12% will result in a gap from the base case that must be addressed either through increased revenues or decreased expenditures. Some of the feasible options for closing the gap are summarized in the following list:

- Revenues
  - Increase Reconstruction Debt Service Offset (REDO) *This has been done in past years, but since a sizeable amount is already assumed to be used each year, increases have tended to be marginal in size.*

- Allocate excess fund balance to reduce the rate requirement. *NOTE: in past years, the Councils have utilized additional excess fund balance to reduce the rate requirement. Council staff believes this action, if required, should be considered at the end of the budget process rather than assumed up front in the spending control limits process. However some amount of fund balance could readily be used to offset some EAM/ERP project costs (as is being done in FY11). This would provide some rate relief in FY12.*

- Expenditures
  - Assume unspecified reductions to be determined later in the budget process
  - Reduce new and expanded programs
  - Reduce compensation assumptions
  - Assume lower "All Other" costs Rate of Increase

In past years, WSSC estimated that approximately 70 percent of its budget involves costs that would be extremely difficult if not impossible to cut in the short-term. Three items alone, debt service, regional sewage disposal, and heat, light, and power, make up 47 percent of the FY12 base case expenditure assumptions and increases in these categories require a 7.4 percent rate increase when combined with revenue adjustments from FY11.

Council Staff Recommendations

Given WSSC's budget profile discussed earlier (i.e. its high level of fixed and/or mandated costs, its flat revenue projections plus the need to makeup for reduced funds available this year), Council Staff believes a significant rate increase is required to avoid unacceptable impacts on WSSC's mission and its ratepayers.

However, it is also important to consider the fiscal context all County agencies are facing this year. County Government and the other agencies will likely need to make substantial cuts in programs and compensation for FY12 on top of major cuts in FY11.

Council Staff supports the County Executive recommended limits:

New Debt:	**$325.285 million**
Debt Service:	**$196.290 million**
Total W/S Operating Expenses:	**$569.513 million**
Maximum Average Rate Increase:	**9.9 percent**

Council Staff believes these recommended limits provide a reasonable ceiling for WSSC and will require WSSC to prioritize its "new and expanded" program needs in the context of its current operating needs. Overall, the 9.9 percent rate increase would require WSSC to find nearly $10.1 million in reductions from its base case scenario and about $3.5 million from its estimated "same services plus CIP" budget. Council Staff supports the County Executive's guidance to WSSC to not reduce its large diameter pre-stressed concrete cylinder pipe (PCCP) inspection, repair, and fiber optic cabling program, nor its water and sewer main reconstruction programs.

Attachments
KML:f:\levchenko\wssc\spending control limits\fy12scl\t&e scl12 10 21 10.doc

ASSUMPTIONS
WSSC's Multi-Year Financial Forecast
FY 2012 thru 2017 Forecast : Preliminary (Revised)

	FY 2012 Proposed	FY 2013 Estimate	FY 2014 Estimate	FY 2015 Estimate	FY 2016 Estimate	FY 2017 Estimate
WATER PRODUCTION						
Yearly Growth Increment (MGD)	-	0.5	0.5	0.5	0.5	0.5
Estimated Annual Average Water Production (MGD)	170.0	170.5	171.0	171.5	172.0	172.5
OPERATING FUNDS						
Salaries & Wages Rate of Increase	5.0%	5.0%	5.0%	5.0%	5.0%	5.0%
Heat, Light & Power Annual Expenses (Includes savings from Energy Performance Program)						
Water ($ thousands)	15,821	14,463	15,354	16,304	17,310	18,409
Sewer ($ thousands)	12,944	11,834	12,563	13,339	14,163	15,062
Blue Plains (Regional Sewage Disposal) Rate of Increase	3.7%	3.7%	3.7%	3.7%	3.7%	3.7%
All Other - % Annual Increase	5.00%	5.00%	5.00%	5.00%	5.00%	5.00%
GASB 045 Expense	7,000	8,000	9,000	10,000	10,000	10,000
Water REDO ($ thousands)	5,500	5,500	5,300	5,300	5,000	5,000
Sewer REDO ($ thousands)	5,500	5,500	5,200	5,200	5,000	5,000
Work Years / FTE $s	-	-	-	-	-	-
Operating Program	-	-	-	-	-	-
Capital Programs	-	-	-	-	-	-
BOND FUNDS						
Short-term Construction Note Rate	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%
Long-Term Bond Interest Rate	6.0%	6.0%	6.0%	6.0%	6.0%	6.0%
Bond Life for Water and Sewer Bonds (yrs)	19	19	19	19	19	19
CAPITAL EXPENDITURES RELATED PARAMETERS						
Construction Inflation	3.0%	3.0%	3.0%	3.0%	3.0%	3.0%
Water Construction Completion Factor	80%	80%	80%	80%	80%	80%
Sewer Construction Completion Factor	80%	80%	80%	80%	80%	80%
Blue Plains Sewer Construction Completion Factor	80%	80%	80%	80%	80%	80%
ENR Construction Completion Factor	80%	80%	80%	80%	80%	80%
Reconstruction Completion Factor	100%	100%	100%	100%	100%	100%

Assumptions

-

WSSC's Multi-Year Financial Forecast : Combined Water/Sewer Operating Funds Summary

FY 2012 thru 2017 Forecast : Preliminary w/ Additional & Reinstated Programs

Estimated Revenues and Expenditures ($1,000)

		FY 2011 Approved	FY 2012 Proposed	FY 2013 Estimate	FY 2014 Estimate	FY 2015 Estimate	FY 2016 Estimate	FY 2017 Estimate
2	**Revenue**							
2	Water & Sewer Rate Revenue	$478,818	$471,636	$529,968	$580,062	$631,097	$672,849	$719,248
3	All Other Sources	51,659	51,186	52,297	50,057	50,611	50,732	50,959
4	Total Revenue	530,477	522,822	582,265	630,119	681,708	723,581	770,207
5	**Expenses**							
6	Maintenance & Operating	320,708	343,725	356,301	371,606	387,547	406,775	427,041
7	Regional Sewage Disposal	47,713	49,478	51,309	53,207	55,176	57,218	59,335
8	Debt Service	174,454	196,290	232,144	264,929	288,948	313,130	337,749
9	PAYGO	-	-	-	-	-	-	-
10	Additional Operating Reserve Contribution	1,500	3,400	4,100	1,500	1,500	1,500	1,500
11	Adjustments to Expenses (SDC Debt Service Offset, REDO)	(13,898)	(13,293)	(13,192)	(11,928)	(11,667)	(10,728)	(10,207)
12	Unspecified reductions	-	-	-	-	-	-	-
13	Total Expenses	$530,477	$579,600	$630,663	$679,314	$721,504	$767,895	$815,419
14	Revenue Gap (Revenue - Expenses)	-	(56,778)	(48,397)	(49,195)	(39,796)	(44,313)	(45,212)
15	**Water Production (MGD)**	170.0	170.0	170.5	171.0	171.5	172.0	172.5
16	**Debt Service Ratio (debt service / budget)**	32.9%	33.9%	36.8%	39.0%	40.0%	40.8%	41.4%

Base Case

		FY 2011	FY 2012	FY 2013	FY 2014	FY 2015	FY 2016	FY 2017
17	Rate Increase	8.5%	12.0%	9.1%	8.5%	6.3%	6.6%	6.3%
18	Operating Budget	$530,477	$579,600	$630,663	$679,314	$721,504	$767,895	$815,419
19	Debt Service Expense	174,454	196,290	232,144	264,929	288,948	313,130	337,749
20	New Debt	249,374	325,285	401,889	341,560	284,930	293,573	307,784

	NOTE:	FY 2011	FY 2012	FY 2013	FY 2014	FY 2015	FY 2016	FY 2017
21	**Impact of Rate Increase on Average Residential Monthly Bill**	***$4.60***	***$7.19***	***$6.11***	***$6.19***	***$4.99***	***$5.55***	***$5.64***

(2)

WSSC's Multi-Year Financial Forecast : Combined Water/Sewer Operating Funds Summary

FY 2012 thru 2017 Forecast : Preliminary w/ Additional & Reinstated Programs

Estimated Revenues and Expenditures ($1,000)

Base Case (Detail)

		FY 2011 Approved	FY 2012 Proposed	FY 2013 Estimate	FY 2014 Estimate	FY 2015 Estimate	FY 2016 Estimate	FY 2017 Estimate
	REVENUE							
1	Water / Sewer Use Charges	$478,818	$471,636	$529,968	$580,062	$631,097	$672,849	$719,248
2	Account Maintenance Fee (Ready to Serve Charge)	22,850	22,850	22,900	22,900	22,950	22,950	23,000
3	Interest Income	4,000	4,000	4,050	4,050	4,100	4,100	4,150
4	Plumbing/Inspection Fees	5,823	5,823	5,873	5,873	5,923	5,973	6,023
5	Rockville Sewer Use	2,258	2,353	2,404	2,444	2,438	2,509	2,536
6	Products & Technology	-	-	-	-	-	-	-
7	Miscellaneous	13,547	12,760	12,970	13,290	13,700	13,700	13,750
8	Total Revenue	527,296	519,422	578,165	628,619	680,208	722,081	768,707
9	**Adjustments to Revenue**							
10	Use of Fund Balance	3,181	3,400	4,100	1,500	1,500	1,500	1,500
11	Less Rate Stabilization	-	-	-	-	-	-	-
12	Adjustments to Total Revenue	3,181	3,400	4,100	1,500	1,500	1,500	1,500
13	**FUNDS AVAILABLE**	530,477	522,822	582,265	630,119	681,708	723,581	770,207
14	**EXPENDITURES**							
15	Salaries and Wages	93,483	98,158	103,067	108,222	113,634	119,317	125,284
16	Salaries and Wages - Additional & Reinstated Programs	-	2,346	2,464	2,588	2,718	2,854	2,998
17	Heat, Light and Power	27,819	28,765	26,297	27,917	29,643	31,473	33,471
18	Regional Sewage Disposal	47,713	49,478	51,309	53,207	55,176	57,218	59,335
19	All Other	199,406	210,182	219,985	228,167	236,604	247,935	259,832
20	All Other - Additional & Reinstated Programs	-	4,274	4,488	4,712	4,948	5,196	5,456
21	Additional Operating Reserve Contribution	1,500	3,400	4,100	1,500	1,500	1,500	1,500
22	Unspecified reductions	-	-	-	-	-	-	-
23	Unspecified reduction of future year's expenditure base	-	-	-	-	-	-	-
24	**Total Operating Expenses**	369,921	396,603	411,710	426,313	444,223	465,493	487,876
25	Debt Service	174,454	196,290	232,144	264,929	288,948	313,130	337,749
26	Debt Reduction (PAYGO)	-	-	-	-	-	-	-
27	**Total Financial Expenses**	174,454	196,290	232,144	264,929	288,948	313,130	337,749
28	**TOTAL GROSS EXPENSES (Operating & Financial)**	544,375	592,893	643,855	691,242	733,171	778,623	825,626
29	Less: SDC Debt Service Offset	(2,398)	(2,293)	(2,192)	(1,428)	(1,167)	(728)	(207)
30	Reconstruction Debt Service Offset	(11,500)	(11,000)	(11,000)	(10,500)	(10,500)	(10,000)	(10,000)
31	**NET EXPENSES**	530,477	579,600	630,663	679,314	721,504	767,895	815,419
32	Revenue - Expenditure Gap before rate increase	-	(56,778)	(48,397)	(49,195)	(39,796)	(44,313)	(45,212)
33	Rate Increase	8.5%	12.0%	9.1%	8.5%	6.3%	6.6%	6.3%

Rate Increase Components

	FY 2011 Approved	FY 2012 Estimate	Dollar Change	Rate Impact	Description
Debt Service	174,454,000	196,290,000	21,836,000	4.63%	Debt Service is increasing due to increased capital spending assumptions (current & prior).
All Other	193,406,000	203,182,000	9,776,000	2.07%	Assumed 5 % increase in All Other Costs
Water & Sewer Revenue	$478,818,000	$471,636,000	$ (7,182,000)	1.52%	Decrease in billing factor. No increase in water production.
Salaries & Wages	93,483,000	98,158,000	4,675,000	0.99%	Assumed 5% increase in Salaries & Wages
Additional & Reinstated Programs		3,570,219	3,570,219	0.76%	
New Positions		3,048,343	3,048,343	0.65%	
Regional Sewage Disposal	47,713,000	49,478,000	1,765,000	0.37%	
Use of Prior Year Net Revenue to fund EAM/ERP	1,681,000	-	(1,681,000)	0.36%	
GASB 45	6,000,000	7,000,000	1,000,000	0.21%	Fifth year of eight year phase-in of GASB 45
Heat, Light & Power	27,819,000	28,765,000	946,000	0.20%	Based on projection from WSSC Energy Manager.
Miscellaneous Revenue	21,628,000	20,936,000	(692,000)	0.15%	Based on historical miscellaneous revenue
Reconstruction Debt Service Offset	11,500,000	11,000,000	(500,000)	0.11%	
SDC Debt Service Offset	2,398,000	2,293,000	(105,000)	0.02%	
				12.04%	

Increased FY'12 Expenditure Assumptions Over and Above Inflation Factor

FY'12 Additional & Reinstated Programs:

New Workyears

Rank	
	Plant Operations
1	1 Sr. Water Plant Operator
2	1 Sr. Mechanical Engineer
3	1 Electrical Mechanical Supervisor
4	1 Facility Technician I
5	1 Electrical Mechanical Technician
	PCCP & Transmission Main Inspection
6	5 Utility Technician
	Water Main Best Practice / Small Valve Exercising & Repair
7	3 Utility Technician
	Leak Detection
8	2 Utility Technician
	Consent Decree - Sewer Design Program - no additional w/s impact - already in CIP
9	4 Project Manager I*
10	3 Project Manager II*
	Water Main & Vault Meter Replacement - no additional w/s impact - already in CIP
11	2 Project Manager I
12	1 Project Manager II
	Utility Master Plan
13	1 Capital Cost Benefit Manager
13	1 Maintenance Electrical Mechanical Engineering Unit Coordinator
13	1 Principal Materials Engineer
13	1 Sr. Civil Engineer - Pipelines
13	2 Buried Asset Strategy Manager
13	1 Maintenance Optimization Manager
13	1 Asset Management Business Improvement Manager
13	1 Buried Systems Manager
13	1 Water Analysis Unit Coordinator
13	1 Principal Civil Engineer
13	1 Engineering Assistant IV
	Geographical Information System
14	1 GIS Program Analyst
	Permit Services
15	1 Permit Agent
	Collections
16	2 Collection Field Specialist
	Site Utility Inspection - fee based
17	1 Contract Manager
	Property & Right of Way Acquisition
18	1 Property Acquisition Agent
	Maintenance
19	1 Customer Care (Maintenance) Unit Coordinator
	Information Technology
20	1 Data Network Engineer
21	1 Sr. FIS Support Developer
	Cross Connection
22	1 Sr. Plumbing Inspector
22	4 Plumbing Inspector
22	1 Inspection Service Agent
	52 Total Workyears

		Cost	W/S Impact
	New Workyears Impact	$ 3,276,200	$ 2,344,879
	Benefits	982,860	703,464
	Miscellaneous Support Equipment	131,570	94,169
Other Additional & Reinstated Programs			
1	570kVA generator	150,000	18,750
2	Corrosion Monitoring Program support	500,000	500,000
3	Chemical Root Control*	500,000	500,000
4	Large Diameter Sewer Main Inspection	1,500,000	1,200,000
5	Geographical Information System Regional Cost Share	100,000	100,000
6	Site Utility Inspection (fee based)	500,000	-
7	Contamination Rapid Response Team Call Back Duty Program	50,000	50,000
8	Lateral Inspection Program	187,500	187,500
9	Generator Fuel Management Program	150,000	150,000
10	Fire Hydrant Painting	200,000	200,000
11	Oracle Master Data Management	500,000	410,000
12	WSSC Messaging & Initiatives Resulting from Customer Survey	200,000	159,800
	Total Other Additional & Reinstated Programs	4,537,500	3,476,050
	Total Additional & Reinstated Programs	**$ 8,928,130**	**$ 6,618,561**

* Consent Decree required.

Additional & Reinstated Summary List.xls

Bud, Fin + Econ Dev.

KL
cc
SBF
LL
GO

058923

RECEIVED
MONTGOMERY COUNTY
COUNCIL
2010 OCT -4 PM 1:49

Isiah Leggett
County Executive

OFFICE OF THE COUNTY EXECUTIVE
ROCKVILLE, MARYLAND 20850

MEMORANDUM

October 4, 2010

TO: Nancy Floreen, President, County Council

FROM: Isiah Leggett, County Executive

SUBJECT: Washington Suburban Sanitary Commission (WSSC) Spending Affordability Limits for the FY12 Operating and Capital Budgets

In April 1994, the Council adopted Resolution No. 12-1558 which established a spending affordability process for the WSSC budget. Under this process, representatives of Montgomery and Prince George's counties meet to develop spending limits for WSSC's upcoming capital and operating budgets. The spending affordability controls consist of limits on the maximum average rate increase, debt service, new debt, and total water and sewer operating expenses. In practice, the greatest amount of attention is focused on the maximum average rate increase, which has the greatest direct effect on WSSC's customers.

A bi-county working group met with WSSC officials and staff on September 8 and September 22 to discuss a variety of spending affordability scenarios. We subsequently received and reviewed additional information from WSSC regarding these and other scenarios.

WSSC faces continuing budget pressures from the escalating costs of chemicals, regional sewage disposal, debt service, and other items, flat or declining water and sewer receipts, and the need to comply with the demands of the SSO Consent Decree. On the other hand, WSSC's customers continue to deal with the painful effects of a persistently weak economy.

While all of these factors need to be considered in determining spending affordability limits for WSSC, our primary concern must be to ensure that the production and distribution of water and the collection and treatment of wastewater remain safe, reliable, and sufficient to meet the needs of County residents. Based on these and related considerations, plus a review of the options developed by the bi-county working group, I recommend the following spending affordability limits for WSSC's FY12 operating and capital budgets:

Maximum Average Rate Increase:	9.9%
Debt Service:	$196,290,000
New Debt:	$325,285,000
Total Water and Sewer Operating Expenses:	$569,513,000

This recommendation strikes a balance between meeting WSSC's urgent needs and limiting the pressure on customer budgets. The maximum average rate increase of 9.9% is the same maximum increase I recommended for last year's spending affordability limits and which the Council subsequently approved. It would represent a 1.4 percentage point increase over the 8.5% rate increase that was ultimately adopted for WSSC's FY11 budget and would add $5.92 to the monthly bill for the average residential customer.

Even with a 9.9% rate increase, WSSC will have to make almost $3.5 million in unspecified spending reductions to balance its budget.[1] I urge that in identifying those reductions, the Commission ensure that the following key programs are preserved:

- The inspection, repair, and fiber optic cabling of large pre-stressed concrete cylinder pipes, and

- The reconstruction and rehabilitation of WSSC's aging small water and sewer mains.

These infrastructure initiatives must remain high priorities to ensure the health and safety of the residents of both counties. Indeed, it is imperative that we identify a stable source of funding for rehabilitating WSSC's underground infrastructure. I remain committed to working with Prince George's County and the Commission to find a way to address this pressing need.

As always, Executive Branch staff stand ready to assist you in your deliberations. I look forward to discussing these issues with you as you develop WSSC's FY12 spending affordability limits.

IL:jfb

c: Commissioner Dr. Roscoe M. Moore, Jr., Vice Chair, Washington Suburban Sanitary Commission
Commissioner Gene W. Counihan, Washington Suburban Sanitary Commission
Commissioner Adrienne A. Mandel, Washington Suburban Sanitary Commission
Jerry Johnson, General Manager/CEO, Washington Suburban Sanitary Commission
Timothy L. Firestine, Chief Administrative Officer
Joseph F. Beach, Director, Office of Management and Budget
Robert Hoyt, Director, Department of Environmental Protection
Stephen Farber, Staff Director, Montgomery County Council
Keith Levchenko, Council Staff
Dave Lake, Department of Environmental Protection
John Greiner, Office of Management and Budget

---

[1] WSSC projects that an average rate increase of 10.6% would be needed to support a budget that preserves current services while funding its proposed FY12-17 CIP. That budget would not include any of the new or reinstated programs and staffing that WSSC believes are needed to meet its expanding obligations and most pressing needs.